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7  
8 IN THE UNITED STATES BANKRUPTCY COURT  
9 FOR THE DISTRICT OF OREGON

10 In re

11 Salpare Bay, LLC,

12 Debtor.  
13  
14

Case No. 10-35333-tmb11

DEBTOR'S FIRST AMENDED CHAPTER 11  
DISCLOSURE STATEMENT (~~SEPTEMBER~~  
~~7, 2010~~APRIL 8, 2011)

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1           **I. INTRODUCTION AND SUMMARY OF PLAN**

2           **A. INTRODUCTION**

3           On June 7, 2010 (the "Petition Date"), Salpare Bay, LLC ("Debtor" or "Salpare")  
4 filed a voluntary petition under chapter 11 of Title 11 of the United States Code (the  
5 "Bankruptcy Code"). The Debtor is seeking acceptance of Debtor's Plan of Reorganization (the  
6 "Plan") by the creditors of the Debtor's estate. This Disclosure Statement (the "Disclosure  
7 Statement") describes:

- 8           • Historical information regarding the Debtor and the events leading to its  
9 bankruptcy filing.  
10           • Significant events since the bankruptcy filing.  
11           • How the Plan proposes to treat claims of the type you hold (i.e., what you  
12 will receive on your claim if the Plan is confirmed).  
13           • Who can vote on or object to the Plan.  
14           • What factors the Bankruptcy Court (the "Court") will consider when  
15 deciding whether to confirm the Plan.  
16           • Why the Debtor believes the Plan is feasible, and how the treatment of  
17 your Claim under the Plan compares to what you would receive on your Claim in liquidation.  
18           • The effect of confirmation of the Plan.

19           A copy of the Debtor's Chapter 11 Plan (the "Plan") is attached hereto as Exhibit  
20 1. You are urged to review the Plan and, if appropriate, consult with counsel about the Plan and  
21 its impact on your legal rights before voting on the Plan. Capitalized terms used but not defined  
22 in this Disclosure Statement shall have the meanings assigned to such terms in the Plan or the  
23 Bankruptcy Code.  
24

25           This Disclosure Statement has been prepared by the Debtor based upon its  
26 knowledge and information in Debtor's books and records. The information contained herein

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1 has been prepared in good faith, based upon information available. The information concerning  
 2 the Plan has not been subject to a verified audit. The Debtor believes this Disclosure Statement  
 3 complies with the requirements of the Bankruptcy Code.

4 The statements contained in this Disclosure Statement are made as of the date  
 5 hereof, unless another time is specified herein, and the delivery of this Disclosure Statement shall  
 6 not imply that there has been no change in the facts set forth herein since the date of this  
 7 Disclosure Statement and the date of the material relied on in preparation of this Disclosure  
 8 Statement was compiled. The description of the Plan contained in this Disclosure Statement is  
 9 intended as a summary only and is qualified in its entirety by reference to the Plan itself. If any  
 10 inconsistency exists between the Plan and this Disclosure Statement, the terms of the Plan are  
 11 controlling. Each holder of a Claim is encouraged to read, consider and carefully analyze the  
 12 terms and provisions of the Plan.

13 This Disclosure Statement may not be relied on for any purpose other than to  
 14 determine how to vote on this Plan. Nothing contained herein shall constitute an admission of  
 15 any fact or liability by any party, or be admissible in any proceeding involving Debtor or any  
 16 other party, or be deemed conclusive advice on the tax or other legal effects of the reorganization  
 17 on the holders of Claims or Interests.

18 The Debtor submits this Disclosure Statement in accordance with Section 1125 of  
 19 the Bankruptcy Code and Bankruptcy Rule 3016. The Bankruptcy Court has scheduled a  
 20 hearing on confirmation of the Plan to commence on \_\_\_\_\_, ~~2010~~2011 at \_\_\_\_\_. The  
 21 Bankruptcy Court will hold that hearing at the United States Bankruptcy Court for the District of  
 22 Oregon, Courtroom No. 4, 1001 SW Fifth Avenue, Portland, Oregon 97204 before the  
 23 Honorable Trish M. Brown. The hearing on confirmation may be adjourned from time to time  
 24 by the Bankruptcy Court without further notice, except for an announcement made at the hearing  
 25 or any adjournment thereof.

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A ballot has been enclosed with this Disclosure Statement for use in voting on the Plan. In order to be tabulated for purposes of determining whether the Plan has been accepted or rejected, ballots must be received at the address indicated on the ballot no later than 4:00 p.m. on \_\_\_\_\_, ~~2010~~, 2011.

## B. SUMMARY OF PLAN

A copy of the Plan is attached hereto as Exhibit 1. The following description of the Plan is intended as a summary only and is qualified in its entirety by reference to the Plan. The Debtor urges each holder of a Claim to carefully review the entire Plan, together with this Disclosure Statement, before voting on the Plan.

~~The~~ Through a mediation held on various dates with the Honorable Michael R. Hogan ("Judge Hogan") between the Debtor ~~will refinance the Property through an FHA loan,~~<sup>1</sup> J.E. Dunn Northwest, Inc. ("Dunn"), the other Secured Creditors with Construction Lien Claims ("Construction Creditors"), Harbor and the City of Portland (collectively the "Parties"), the Parties reached a settlement regarding their disputes, the claims between them related to the Project and the pending bankruptcy proceedings (the "Settlement Agreement"). Pursuant to the Settlement Agreement, the Settlement Parties consent to confirmation of the Plan on the terms set forth herein. A copy of the Settlement Agreement is attached hereto as Exhibit 2.

The general terms of the Settlement Agreement include the Construction Creditors and the City of Portland receiving payments equal to 88.26% of their judgment amounts inclusive of principal, fees, costs and interest as of March 31, 2011<sup>1</sup> ~~which will allow the Debtor to develop~~ (the "Discounted Judgment Amount") in three installments on or before the following dates: June 30, 2012; October 31, 2012 and June 30, 2013. Interest shall accrue on the Discounted Judgment Amount at the rate of 3.25% per annum from the Effective Date. As

<sup>1</sup> ~~Alternatively, the Debtor will obtain a conventional loan to develop~~ The total judgment amount claimed by the Construction Creditors and the City of Portland is set forth on Exhibit A to the ~~Property. See Section VI.B.1 for further discussion.~~ Settlement Agreement.

part of the Settlement Agreement, the principals of Harbor, George Killian and Lance Killian, shall convey their membership interests in Harbor to the Debtor and, as inducement for the Debtor to accept that assignment, George Killian and Lance Killian shall pay \$40,000 to the Debtor.

The Debtor will commence development of the Property by first obtaining a priming loan with a maximum amount of \$500,000 (with leave to seek an additional \$250,000) to prepare the Property for the development of a multi-family residential project in two (2) phases around the Marina, and second, through an FHA loan to commence construction on phase 1.<sup>2</sup> The funding for that development will allow the Debtor to develop, with Creditors holding Allowed and Claims secured by perfected construction liens<sup>3</sup> to be paid in full by June of 2013. Creditors with Unsecured Claims will be paid ~~from either or both additional loan proceeds or Net Operating~~ on their Allowed Claims a pro rata amount quarterly commencing after June 30, 2012, from 30% of Net Income through the end of 2017 (to the extent it does not cause the Debtor to default under its loan documents and to the extent the Debtor's ending cash balances exceed \$500,000) generated by the Debtor post-confirmation.

The only Secured Creditors in this case are the county taxing authorities and Creditors asserting that they hold a Claim secured by a perfected Construction Lien asserted under Oregon law or by judgment. The Debtor will develop the Property with three distinct sections, and to the extent necessary, will partition the Property into three ~~ways~~ separate portions: (1) the Marina; (2) Phase 1;<sup>24</sup> and (3) Phase 2.<sup>3</sup> ~~The FHA lender will~~<sup>5</sup> The Debtor is working

<sup>2</sup> Alternatively, the Debtor will obtain a conventional loan to develop the Property.

<sup>3</sup> Dunn contends that the constructions liens asserted by Secured Creditors are perfected, have been foreclosed and that such liens constitute state court judgment liens against the Property.

<sup>24</sup> The Debtor intends to develop the first phase of the multi-family residential project with approximately 166 apartment units and ancillary improvements where Building C currently sits on the Property, as indicated on Exhibit ~~23~~ hereto.

1 with land use attorney, Dorothy Cofield, to either partition the Property or obtain verification  
 2 from the City of Portland, that a partition is not necessary to allow a lender or Secured Creditor  
 3 to foreclose on a portion of the Property subject to a trust deed or lien and obtain a division or  
 4 unit of land that is not a partition but can be deeded to a separate owner after foreclosure. The  
 5 City of Portland has confirmed the latter and that it will continue to apply the past land use  
 6 approvals to the entire site, notwithstanding a foreclosure on a portion of the Property and, thus,  
 7 if the FHA lender approves, then a partition may not be necessary, which will save significant  
 8 costs to the estate. The Marina condominium plat will be finalized and recorded with the State  
 9 of Oregon to effect a division of the marina property from the upland multi-family property.

10 Under the Settlement Agreement, the Parties have agreed that the Debtor shall  
 11 obtain a maximum loan of \$500,000, which shall be secured with a trust deed to which the  
 12 Construction Creditors will subordinate their liens (the "Priming Loan"), to put in a parking lot  
 13 for the Marina, possibly partition the Property as set forth above, and to develop the Property  
 14 sufficient to obtain the FHA loan on Phase 1 (surveying, engineering and other related  
 15 costs/expenses). The Construction Claimants may consider an additional \$250,000 addition to  
 16 the Priming Loan upon receipt of a fully executed commitment letter from a bank or other  
 17 financial institution agreeing to loan the Debtor the funds necessary to construct Phase 1 of the  
 18 Project.

19 Upon the closing of the FHA loan on Phase 1, the Construction Creditors will  
 20 release their liens on Phase 1 to allow the FHA lender to obtain a first lien ~~on Phase 1 of~~ upon the  
 21 Property, subject to payment of the amounts set forth herein to those Secured Creditors with  
 22 Construction Lien Claims. Upon the closing of the FHA loan, ~~on Phase 1,~~ and when the Debtor

23 <sup>3</sup> ~~Phase 2 means the development of the remainder of the planned approximately 371 multi-family~~  
 24 ~~residential units as indicated on Exhibit 2 hereto.~~

25 <sup>5</sup> Phase 2 means the development of the remainder of the planned approximately 371 multi-family  
 26 residential units as indicated on Exhibit 3 hereto.

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1 makes its initial payment to the ~~Creditors holding a claim secured by an Allowed~~ Construction  
 2 ~~Lien~~ Creditors, each such Claimant will retain its lien on the Marina and Phase 2 with the same  
 3 priority such lien had on the Petition Date. The Debtor will refinance the Marina and make  
 4 another payment to the Construction Creditors by October 31, 2011, at which time those  
 5 Claimants will release their liens on the Marina. Such Claimants will be paid in full by June of  
 6 2013 from loan proceeds obtained by the Debtor. Small creditors with Unsecured Claims equal  
 7 to or less than \$2,000 will be paid 100% of their Allowed Claim in Cash, with 25% being paid  
 8 ~~within sixty (60) days of the Effective Date of the Plan~~ October 31, 2012 and the remaining 75%  
 9 being paid on or before ~~October 31, 2011~~ June 30, 2013. Creditors holding General Unsecured  
 10 Claims will receive Pro Rata distributions of 30% of Net ~~Operating~~ Income generated by the  
 11 Reorganized Debtor on a quarterly basis for five (5) years, ~~ending December 31, 2016~~. All post-  
 12 petition and Administrative Expense Claims will be paid upon the Effective Date unless such  
 13 ~~claimant~~ Claimant agrees to different treatment in writing. All current equity interests will ~~be~~  
 14 ~~cancelled and new equity may be issued as set forth in more detail in the Plan.~~ either be retained  
 15 by the current owner, Mr. DeFrees, or transferred to the Debtor by the owners of Harbor, as set  
 16 forth herein. Mr. DeFrees shall retain his current equity interests in exchange for his  
 17 subordination of his \$10,900,000 General Unsecured Claim.

18 All unexpired leases and executory contracts will be rejected by the Debtor  
 19 through the Plan unless such unexpired leases and executory contracts have previously been  
 20 assumed and assigned, or rejected, or a motion seeking their assumption or rejection has been  
 21 Filed before the Confirmation Date.

22 The Effective Date of the Plan shall be \_\_\_\_\_, ~~20~~ 2011 or the 10th day  
 23 following entry of the Confirmation Order, whichever is later.

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1 In the event that any Class of Creditors of the Debtor does not accept the Plan, the  
 2 Debtor reserves the right to request that the Bankruptcy Court confirm the Plan in accordance  
 3 with Section 1129(b) of the Bankruptcy Code or otherwise modify the Plan.

#### 4 **C. BRIEF EXPLANATION OF CHAPTER 11**

5 Chapter 11 of the Bankruptcy Code is the principal reorganization provision of  
 6 the Bankruptcy Code. Pursuant to Chapter 11, a debtor attempts to reorganize its business for  
 7 the benefit of the debtor, its creditors, and other parties in interest.

8 The formulation and confirmation of a plan of reorganization is the principal  
 9 purpose of a Chapter 11 case. A plan of reorganization sets forth a proposed method for  
 10 compensating the holders of claims and interests in the debtor. A claim or interest is impaired  
 11 under a plan of reorganization if the plan provides that the legal, equitable or contractual rights  
 12 of the holder of such claim or interest are altered. A holder of an impaired claim or interest is  
 13 entitled to vote to accept or reject the plan. Chapter 11 does not require all holders of claims and  
 14 interests to vote in favor of a plan in order for the Bankruptcy Court to confirm it. However, the  
 15 Bankruptcy Court must find that the plan meets a number of statutory tests before it may approve  
 16 the plan. These tests are designed to protect the interests of the holders of claims or interests  
 17 who do not vote to accept the plan, but who will nonetheless be bound by the plan's provisions if  
 18 it is confirmed by the Bankruptcy Court.

19 An official committee of unsecured creditors is appointed by the United States  
 20 Trustee's office in most Chapter 11 cases to, among other things, negotiate the plan of  
 21 reorganization on behalf of the unsecured creditors of the debtor. A committee of unsecured  
 22 creditors was not appointed by the United States Trustee in this case.

## 23 **II. VOTING PROCEDURES AND CONFIRMATION OF A PLAN.**

### 24 **A. BALLOTS AND VOTING DEADLINE**

1 A ballot to be used for voting to accept or reject the Plan is enclosed with each  
2 copy of this Disclosure Statement mailed to all Creditors entitled to vote. After carefully  
3 reviewing this Disclosure Statement and its exhibits, including the Plan, please indicate your  
4 acceptance or rejection of the Plan by voting in favor or against the Plan on the enclosed ballot as  
5 directed below.

6 The Bankruptcy Court had directed that, to be counted for voting purposes, ballots  
7 for acceptance or rejection of the Plan must be received no later than 4:00 p.m. Pacific time, on  
8 \_\_\_\_\_, 2010 by the Debtor at the following address:

9 Farleigh Wada Witt  
10 Attn: Diane Fallon  
11 121 SW Morrison, Ste. 600  
Portland, OR 97204

12 or via facsimile transmission to Diane Fallon at (503) 228-1741, or via e-mail in  
13 pdf format to dfallon@fwwlaw.com.

14 Holders of each Claim that was scheduled by the Debtor or with respect to which  
15 a Proof of Claim has been Filed for which no objection is pending will receive ballots and are  
16 permitted to vote based on the amount of the Proof of Claim. If no Proof of Claim has been  
17 Filed, then the vote will be based on the amount scheduled by the Debtor in its Schedules.  
18 Holders of Disputed Claims who have settled their dispute with the Debtor are entitled to vote  
19 the settlement amount of their Claim. The Bankruptcy Code provides that such votes will be  
20 counted unless the Claim has been disputed, disallowed, disqualified or suspended prior to  
21 computation of the vote on the Plan. The Claim to which an objection has been Filed is not  
22 allowed to vote unless and until the Bankruptcy Court rules on the objection. The Bankruptcy  
23 Code provides that the Bankruptcy Court may, if requested to do so by the holder of such claim,  
24 estimate or temporarily allow a Disputed Claim for the purposes of voting on the Plan.

25  
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1 If a person holds Claims in more than one class entitled to vote on the Plan, such  
2 person will be entitled to complete and return a ballot for each Class. If you do not receive a  
3 ballot or if a ballot is damaged or lost, please contact:

4 Farleigh Wada Witt  
5 Attn: Diane Fallon  
6 121 SW Morrison, Ste. 600  
Portland, OR 97204  
Telephone Number: (503) 228-6044

7 All persons entitled to vote on the Plan may cast their vote for or against the Plan  
8 by completing, dating and signing the enclosed ballot and returning it, by First Class Mail or  
9 hand delivery, to the Debtor, at the address indicated above. In order to be counted, all ballots  
10 must be executed and received at the above address no later than 4:00 Pacific time on  
11 \_\_\_\_\_, 2010. Any ballots received after 4:00 p.m. Pacific time on \_\_\_\_\_, 2010 will  
12 not be included in any calculation to determine whether the parties entitled to vote on the Plan  
13 have voted to accept or reject the Plan.

14 Ballots may be received by the Debtor by facsimile transmission to Farleigh  
15 Wada Witt, Attn: Diane Fallon at (503) 228-1741. Ballots sent by facsimile transmission will be  
16 counted if faxed to Ms. Fallon by 4:00 p.m. Pacific time on \_\_\_\_\_, 2010.

17 When a ballot is signed and returned without further instruction regarding  
18 acceptance or rejection of the Plan, the signed ballot shall be counted as a vote accepting the  
19 Plan. When a ballot is returned indicating acceptance or rejection of the Plan but is unsigned, the  
20 unsigned ballot will not be included in any calculation to determine whether parties entitled to  
21 vote on the Plan have voted to accept or reject the Plan. When a ballot is returned without  
22 indicating the amount of the Claim, the amount shall be as set forth on the Debtor's Schedules or  
23 any Proof of Claim Filed with respect to such Claim.

24 **B. PARTIES ENTITLED TO VOTE**

Pursuant to Section 1126 of the Bankruptcy Code, each class of impaired claims or interests that is not deemed to reject the Plan is entitled to vote to accept or reject the Plan. Any holder of an Allowed Claim that is in an impaired class under the Plan, and whose Class is not deemed to reject the Plan, is entitled to vote. A Class is "impaired" unless the legal, equitable and contractual rights of the holders of claims in that Class are left unaltered by the Plan or if the Plan reinstates the Claims held by members of such Class by (1) curing any defaults, (2) reinstating the maturity of such claim, (3) compensating the holder of such claim for damages that result from the reasonable reliance on any contractual provision of law that allows acceleration of such claim and (4) otherwise leaving unaltered any legal, equitable or contractual right of which the Claim entitled the holder of such claim. Because of their favorable treatment, classes that are not impaired are conclusively presumed to accept the Plan. Accordingly, it is not necessary to solicit votes from the holders of claims in classes that are not impaired.

Classes of Claims or Interests that will not receive or retain any money or property under a Plan on account of such Claims or Interests are deemed, as a matter of law under Section 1126(g) of the Bankruptcy Code, to have rejected the Plan and are likewise not entitled to vote on the Plan. The current ownership interests classified as Class 10 are such a class and are deemed to have rejected the Debtor's Plan.

Class 1 (Other Priority Creditors) and Class 6 (County Secured Claim for Property Taxes) are not impaired and, therefore, are deemed to have accepted the Plan. All other Classes of Claims are impaired under the Plan, and persons holding Claims are entitled to vote to accept or reject the Plan.

### **C. VOTES REQUIRED FOR CLASS ACCEPTANCE OF THE PLAN**

As a condition to confirmation, the Bankruptcy Code requires that each impaired Class of Claims or Interests accept the Plan, subject to the exceptions described below in the

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1 section entitled "Cram Down of the Plan." At least one impaired Class of Claims must accept  
2 the Plan in order for the Plan to be confirmed.

3 For a Class of Claims to accept a plan, Section 1126 of the Bankruptcy Code  
4 requires acceptance by Creditors that hold at least two-thirds in dollar amount and a majority in  
5 number of the Allowed Claims of such Class, in both cases counting only those claims actually  
6 voting to accept or reject the Plan. If the Plan is confirmed, the Plan will be binding with respect  
7 to all holders of Claims and Interests in each Class, including Classes and members of Classes  
8 that did not vote or that voted to reject the Plan.

#### 9 **D. "CRAM DOWN" OF THE PLAN**

10 If the Plan is not accepted by all of the Impaired Classes of Claims, the Plan may  
11 still be confirmed by the Bankruptcy Court pursuant to Section 1129(b) of the Bankruptcy  
12 Code's "Cram Down" provision if the Plan has been accepted by at least ~~one~~one Impaired Class  
13 of Claims, without counting the acceptances of any Insiders of the Debtor, and the Bankruptcy  
14 Code determines, among other things, that the Plan "does not discriminate unfairly" and "is fair  
15 and equitable" with respect to each non-accepting Impaired Class of Claims or Interests. The  
16 Debtor believes that the Plan can be confirmed even if it is not accepted by all impaired Classes  
17 of Claims.

#### 18 **E. CONFIRMATION HEARING**

19 The Bankruptcy Court has scheduled a hearing on confirmation of the Plan to  
20 commence on \_\_\_\_\_, 2010, at \_\_\_\_\_. The Confirmation Hearing will be held at  
21 the United States Bankruptcy Court for the District of Oregon, Courtroom No. 4, 1001 SW Fifth  
22 Avenue, 9<sup>th</sup> Floor, Portland, Oregon, before the Honorable Trish M. Brown, United States  
23 Bankruptcy Judge. At the hearing, the Bankruptcy Court will consider whether the Plan satisfies  
24 the various requirements of the Bankruptcy Code, including whether it is feasible and whether it  
25 is in the best interests of the creditors of the Debtor. At that time, the Debtor will submit a report  
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1 to the Bankruptcy Court concerning the votes for acceptance or rejection of the Plan by the  
2 persons entitled to vote thereon.

3 Section 1128(b) of the Bankruptcy Code provides that any party in interest may  
4 object to confirmation of the Plan. Any objections to confirmation of the Plan must be made in  
5 writing and filed with the Bankruptcy Court and received by counsel for the Debtor no later than  
6 \_\_\_\_\_, ~~2010, 2011~~, by 4:00 p.m. Pacific time. Unless an objection to confirmation is  
7 timely filed and received, it may not be considered by the Bankruptcy Court.

### 8 **III. BACKGROUND AND GENERAL INFORMATION**

#### 9 **A. PROPERTY DEVELOPMENT**

10 Salpare and Harbor ~~Investors, LLC (“Harbor”)~~ are the owners of real property on  
11 Hayden Island, Portland, Oregon that was to be developed into a luxury riverfront planned  
12 community of 204 high-end residential water view condominium units commonly known as  
13 Salpare Bay (the “Project”). Salpare and Harbor own the Project with an undivided 85% and  
14 15% interest, respectively, pursuant to a ~~joint tenancy agreement.~~ tenancy in common  
15 agreement. However, pursuant to the Settlement Agreement, the owners of Harbor will transfer  
16 their membership interests in Salpare to Salpare; therefore, Harbor will no longer own an interest  
17 in Salpare or the Property.

18 Salpare began construction in approximately 2005 on the related marina and other  
19 horizontal improvements. The Project presently includes 24.5 acres of land, a marina, 200 feet  
20 of beach on the Columbia River, 14 acres of water, 204 slips to accommodate large crafts and  
21 amenities and facilities such as wireless internet, cable television, laundry, showers and dump  
22 station facilities.

23 BankFirst, Inc. (“BankFirst”) was the lead lender of 41 participating lenders who  
24 promised \$63 million in construction financing (the “Loan”) for the Project. However, after it  
25 received nearly \$1 million in loan fees at the closing of the Loan in December 2006, BankFirst  
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1 was dilatory in funding the Loan. Later, in June 2007, it stopped funding the Loan entirely based  
 2 on a pretextual default, claiming Salpare and Harbor had failed to fulfill certain presold unit  
 3 requirements that BankFirst had previously waived on numerous occasions. Moreover,  
 4 BankFirst misled Salpare into proceeding with construction, even though as it turns out,  
 5 ultimately, it had no ability to fund the Loan. Notably, Salpare was in full compliance with the  
 6 Loan terms, including fulfilling all monthly payment obligations.

7 In the meantime, despite Salpare's compliance with the Loan, unbeknownst to the  
 8 guarantor Michael DeFrees ("DeFrees"), BankFirst confiscated DeFrees' \$4 million bank  
 9 account that was provided as additional collateral for the Loan that he had intended to use to  
 10 fund the Project. BankFirst, realizing that it had problems declaring a default under these  
 11 conditions without a release of Salpare's claims, demanded under a threat of default and  
 12 foreclosure, execution of a first amendment of the Loan documents (the "First Amendment") that  
 13 purported to resurrect and reinstate the presale conditions that it waived; required Salpare to  
 14 fulfill the resurrected conditions by selling \$50 million in units in what was ultimately a two-  
 15 week period; retroactively required Salpare to bless BankFirst's unlawful confiscation of  
 16 DeFrees' bank account; and provided for a release and waiver of all claims against BankFirst for  
 17 its wrongful conduct. Salpare and Harbor complained that the First Amendment was impossible  
 18 to fulfill, lacked any consideration and was simply unlawful. BankFirst rejected such  
 19 complaints. BankFirst reiterated its threat of foreclosure and added a promise to negotiate a  
 20 further extension after the First Amendment was executed. Although Salpare executed the First  
 21 Amendment, BankFirst did not negotiate further for an extension as promised.

22 What Salpare and Harbor did not know, and BankFirst did not disclose to them  
 23 during these events, was that BankFirst was having its own financial problems. Within days  
 24 after Salpare and Harbor signed the First Amendment, on August 7, 2007 BankFirst executed  
 25 with the Federal Reserve an agreement ("Consent Order") which limited its funding of future  
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1 loans to the maximum amount on BankFirst's books as of March 12, 2007, which was about the  
 2 time that BankFirst's funding of the Loan slowed nearly to a stop.

3 As a result of BankFirst's failure to fund the Loan, all construction at the Project  
 4 ceased. The contractor ~~JE, Dunn Northwest Inc. ("Dunn"), and other subcontractors (the~~  
 5 ~~"Construction Claimants")~~ subcontractors had performed a substantial amount of work for which  
 6 Salpare could not pay them because of BankFirst's failure to fund the Loan; thus, they filed  
 7 construction liens ~~and on~~ against the Property. On or about October 26, ~~2007. They in turn~~ 2007,  
 8 the Construction Creditors filed an action on their construction claims ("Construction Claims")  
 9 in that case known as *J.E. Dunn Northwest, Inc. v. Salpare Bay, LLC, et. al.* in the Circuit Court  
 10 of the State of Oregon, Multnomah County, Case No. 0710-12536 (the "Dunn Action").  
 11 Thereafter, the Project deteriorated. The sales agents and team quit; purchasers of the presold  
 12 units cancelled their purchases and withdrew their deposits; and the development came to a halt  
 13 in all respects by the end of 2007.

14 In the Dunn Action, BankFirst asserted claims based on the Loan against Salpare,  
 15 Harbor, DeFrees, Columbia Rim Construction, Inc. and Columbia Rim Corporation (collectively,  
 16 the "Salpare Parties"). The Salpare Parties counterclaimed against BankFirst and the participant  
 17 lenders, originally identified only as the "DOES," because their identity was not known. The  
 18 Salpare Parties claimed \$130 million in damages, plus any penalties and attorneys' fees that may  
 19 be awarded for breach of contract, negligence, interference with contract, promissory estoppel,  
 20 conversion, breach of good faith and fair dealing, breach of fiduciary duty, four counts of fraud,  
 21 negligent misrepresentation, rescission and violation of Oregon Racketeer Influenced and  
 22 Corrupt Organization Act.

23 The Dunn Action was bifurcated between the Construction Claims and the Loan  
 24 claims. When a Limited Judgment was about to be entered in the Dunn Action on the  
 25 Construction Claims, BankFirst's assets were seized by the Federal ~~Deposits and~~ Deposit  
 26

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Insurance Corporation ("FDIC"). After the FDIC removed the entire Dunn Action, a Limited Judgment was entered in the Circuit Court of the State of Oregon on September 9, 2009, which Salpare contends had no effect since the Dunn Action had been removed. To further add to the problems with that Limited Judgment, it was entered *nunc pro tunc* to April 21, 2009, thus invalidly cutting off parties' appeal rights. Following the transfer of the Dunn Action back to the Circuit Court of State of Oregon, an Order Reaffirming the Limited Judgment was signed and entered on January 22, 2010, but no separate Limited Judgment was entered on that date and the Order Reaffirming the Limited Judgment did not correct the inappropriate nunc pro tunc entry that cut off parties' appeal rights.

Dunn contends that the method and timing by which the State Court entered the Limited Judgment did not cut off the parties' appeal rights. Dunn contends that there are four key facts concerning the Dunn Action: (1) that the State Court found that the construction liens had priority over BankFirst's position; (2) that the liens cover the entire Property, including the Marina; (3) that Salpare stipulated to the amounts due to the plaintiffs in the Dunn Action; and (4) that the State Court made detailed findings of fact and conclusions of law.

After the Dunn Action was returned to the Circuit Court of the State of Oregon, it was further bifurcated with BankFirst's and the Salpare Parties' claims removed to Federal Court for disposition in the United States District Court for the District of Oregon Case No. 10-373-PK (the "Federal Case"). In those proceedings, the Salpare Parties identified and served the participant lenders requiring that they appear and defend against the Salpare Parties' claims.<sup>46</sup> In the Federal Case, the Salpare Parties and George Killian, (the principal of Harbor) on the one hand, and the FDIC and participants on the other, entered into a settlement on the record on June 2, 2010 that resolved all claims between them. In the meantime, Dunn sought to proceed with an

<sup>46</sup> During the litigation the identity of the participants was learned as the result of an Order obtained by the Salpare compelling BankFirst to provide discovery.

1 execution sale on the Limited Judgment for the Construction Claims, with a foreclosure sale  
2 scheduled for June 8, 2010.

3 The Salpare Parties, the FDIC for BankFirst, and the loan participants entered into  
4 a written settlement agreement on or about June 7, 2010, pursuant to which all parties agreed to  
5 dismiss the Federal Case and the Salpare Parties released their claims against BankFirst, the loan  
6 participants and the FDIC (the "Settlement"). As a result of the Settlement and in consideration  
7 of the Salpare Parties' release of their claims (the value of which was equal to or exceeded the  
8 Loan balance), the FDIC for BankFirst and the loan participants have agreed not to seek payment  
9 on the Loan from Salpare or Harbor. The only Secured Claims against the Property are those  
10 held by construction lien claimants and real property taxing authorities, all totaling  
11 approximately \$7.5 million.

12 Salpare currently operates a high-end marina business with 204 slips on the  
13 Property. The Marina was completed in 2007 and became operational in the Spring of 2007.  
14 The Marina is an extremely attractive and appealing operation situated on the Columbia River,  
15 having been constructed and dredged at significant cost by Salpare. Salpare maintains a  
16 clubhouse for the Marina with laundry, kitchen, bathroom and shower facilities and rents out a  
17 yacht sales office. It contracts for catering events, repair and cleaning of boats and provides  
18 other services and goods for compensation to its lessees. Each slip has dockside access to  
19 electricity, water and internet service. Moreover, the Marina has extrinsic value in that it is the  
20 only marina in Oregon that has fee title ownership for each slip.<sup>7</sup> Therefore, there is an  
21 opportunity for the slips at the Marina to be sold individually and not subject to any leasehold  
22 interest held by a governmental authority.

23 Due to the changes in the overall economic climate since 2005, the Debtor now  
24 plans to construct approximately 371 apartment units on Phase 1 and Phase 2 of the Property.

25 <sup>7</sup> Dunn disagrees that the marina slips may be sold individually.  
26

1 The building pads at Building C for the previously planned condominium project are anticipated  
 2 to serve as the foundation for Phase 1 of the proposed multi-family development. Salpare  
 3 intends to develop the Property in two (2) phases, with the first phase comprised of  
 4 approximately 166 apartment units and ancillary improvements.

5 Salpare currently maintains temporary parking for the Marina on the industrial  
 6 zoned portion of the Property. Salpare has filed an application to construct permanent parking  
 7 for the Marina on the Property and has ~~filed an application to employ~~retained land use counsel,  
 8 Dorothy Cofield, to assist it in obtaining the conditional use application from the City of Portland  
 9 as well as to possibly divide the commercial zoned land from the marina (by either a partition or  
 10 as a unit of land created by a deed of trust metes and bounds legal description), which it believes  
 11 will generate more options for the development of the Property as a multi-family residential and  
 12 marina project.

13 Salpare has ~~begun the process to obtain funding to develop the initial phase of the~~  
 14 ~~Project, and has generated interest from lenders. Salpare has~~a term sheet from a reputable well-  
 15 known lender for the FHA 221(d)(4) of the National Housing Act loan that it seeks to develop  
 16 Phase 1 of the Property (the "FHA Lender"). Salpare hired Obsidian Finance Group early on in  
 17 this case to provide financial consulting services to it in its endeavors to develop the Property  
 18 and obtain financing for it. Salpare ~~has~~ also hired Steven Wiltshire of Marcus & Millichap  
 19 ("M&M"), a financial services broker, ~~who has issued a pre-qualification approval letter and. An~~  
 20 FHA 221(d) mortgage loan is a multifamily construction loan guaranteed by FHA/HUD. Unlike  
 21 some FHA/HUD programs, there is no requirement that the multifamily units be offered at below  
 22 market rents.

23 Salpare's FHA Lender has issued a term sheet to ~~the Debtor for purposes of~~  
 24 ~~funding the development of the Project. That pre-qualification states that M&M is "highly~~  
 25 ~~confident" that the Debtor can successfully obtain~~Salpare for an FHA 221(d) mortgage loan.  
 26

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~~The M&M term sheet provides that Salpare is prequalified for an FHA loan in the amount of \$24,194,000 or 83.3% loan to cost or the minimum of 1.20 Debt Coverage Ratio using market income proforma or validated market income and expense components, whichever is less on the following general terms: (i) a proposed loan amount of \$19,938,200; (ii) a current estimated interest rate of 5.75%; (iii) a construction loan term of the construction period plus four months, interest only; (iv) a permanent loan term of 40 years or 75% of the remaining useful economic life of the Property; (v) no prepayment for 2 years without a fee; (vi) total deposits due at application of \$37,500; (vii) a financing fee of 2% of the loan amount, with a good faith deposit of .5% and a firm commitment application fee of .3%; (viii) secured by a first lien encumbering Phase 1 of the Property.~~ The construction period is to be 14 months to allow for 12 months construction and two months for cost certification, which requires Salpare and the general contractor to submit a cost certification prepared by an independent public accountant upon completion of construction. Upon issuance of a Certificate of Occupancy, the loan will be converted to a 40-year fixed term with a 40-year amortization, with a loan rate of ~~5.15~~5.75%. The loan will be non-recourse. The loan origination fee will be .73% of the loan amount payable at closing of the loan.

Salpare's projections indicate gross potential rental income of \$2.7 million to \$2.9 million for just the first 166 units. While occupancy rates have dropped over the past few years, the market is improving and established multi-family residential developments in the Portland area continue to be feasible.

## **B. MANAGEMENT**

Columbia Rim Corporation ("CR Corp.") is the manager of the Debtor's limited liability company. CR Corp.'s shares are owned 50% by Michael DeFrees ("DeFrees") and 50% by Christy DeFrees. DeFrees runs the day to day operations of CR Corp. DeFrees is the sole member of the Debtor and runs the day to day operations of the Debtor. DeFrees is a native of

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the Vancouver, Washington area and began his career as a developer by building single family residential housing projects in the early 1980s. He then began developing commercial projects and has developed hotels, recreational vehicle parks, medical complexes, and apartment buildings over his 30-year career. DeFrees is not an employee of the Debtor; rather the Debtor pays Gateway National Corporation ("Gateway") for the services provided to it by Gateway's employees, of which DeFrees is one. DeFrees is shareholder and the President of Gateway. The Debtor pays approximately \$5,000 per month for management fees to Gateway for the services DeFrees and others perform on its behalf. DeFrees will continue to oversee the operations of the Debtor and will continue to be paid from his other entities for such services provided.

#### C. FINANCIAL PERFORMANCE

Attached hereto as Exhibit ~~34~~ are the income statements for the Debtor for its fiscal years ending in the prior three years. The income statements reflect the expense associated with the BankFirst related debt and, thus, do not provide an accurate picture of the Debtor's true net income from its current operations because BankFirst no longer seeks payment of that debt pursuant to the Settlement. Additional or more detailed information may be obtained by submitting a written request to Debtor's counsel identifying the information sought.

### IV. THE BANKRUPTCY CASE

#### A. THE FILING

The Debtor filed its voluntary petition for relief under Chapter 11 of the Bankruptcy Code on June 7, 2010.

#### B. POST -PETITION DEVELOPMENTS

After the filing of the Petition, the Debtor sought and obtained the following orders: (1) an Order Pursuant to 11 USC § 366(a) Finding Adequate Assurance of Payment for Future Utility Services (Docket No. 36); (2) an order authorizing the employment of ~~Spencer~~ Powell Valuation, Inc. as an appraiser for the Debtor's Property (Docket No. ~~67~~73); (3) an order

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1 authorizing the employment of Farleigh Wada Witt as counsel for the Debtor (Docket No. 90);  
 2 ~~and~~ (4) an order authorizing the employment of Obsidian Finance Group, LLC ("Obsidian") as a  
 3 financial consultant to the Debtor (Docket No. 80); an order authorizing the employment of  
 4 Marcus & Millichap Capital Corporation as a loan broker to the Debtor (Docket No. 110); and an  
 5 order authorizing the employment of Dorothy Cofield as the Debtor's land use attorney (Docket  
 6 No. 105). Because the BankFirst debt was eliminated prepetition, there was no need for the  
 7 Debtor to obtain an order authorizing use of cash collateral.

8 Almost immediately after the Debtor filed its Petition, Dunn filed a motion for  
 9 relief from stay to foreclose its asserted construction lien against the Property, alleging that there  
 10 was no equity in the Property for the Debtor and that it was not necessary for an effective  
 11 reorganization. After a two-day contested hearing before the Court held on August 3 and 4,  
 12 2010, the Court entered an order denying Dunn's motion and holding that there is equity in the  
 13 Property over the amount of Dunn's asserted secured claim, that the Property is necessary for an  
 14 effective reorganization and that the Debtor did not file this case in bad faith. This Court also  
 15 found that this is a single asset real estate case under 11 USC §101(51B) and that, thus, the  
 16 provisions of 11 USC §362(d)(3) apply.

17 The US Trustee's Office has not appointed an unsecured creditors committee in  
 18 this case.

19 As previously discussed in Section I(B), supra, the Debtor, Harbor and the  
 20 Construction Creditors engaged in lengthy settlement discussions with the assistance of Judge  
 21 Hogan, which culminated in the parties agreeing to the Settlement Agreement attached hereto as  
 22 Exhibit 2. The Settlement Agreement will be the subject of a separate notice of intent to settle  
 23 for this Court's approval. However, assuming that the Settlement Agreement is approved by this  
 24 Court, the Construction Creditors and Harbor have agreed that they will consent to the Debtor's  
 25 Plan.

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1           **V.     ASSETS AND LIABILITIES**

2                   **A.     ASSETS**

3                           **1.     Real Property.**

4                   The Debtor's assets consist primarily of the Property, which is comprised of a  
 5   204-slip, fully operating high-end marina on the Columbia River, a commercially zoned parcel  
 6   of land about 24 acres in size that contains a partially constructed parking garage that may be  
 7   used in the 375-unit apartment complex contemplated by the Debtor's Plan, and an industrially  
 8   zoned parcel of land about 1.8 acres in size that currently houses temporary parking for the  
 9   marina and a high-end sales trailer leased by a yacht sales company, Royal Marine.

10                           **2.     Other Property.**

11                   The Debtor's other assets consist of a claim against its co-owner of the Property,  
 12   Harbor for the amounts Harbor owes it under the joint tenancy agreement. The Debtor ~~has had~~  
 13   sued Harbor to recover on that claim in Adversary Proceeding No. 10-~~03252~~-03252, but that  
 14   claim is to be settled under the Settlement Agreement for the transfer of the Killians'  
 15   membership interests in Harbor to Salpare and, as inducement for Salpare to accept such  
 16   assignment, payment by Harbor to Salpare of \$40,000. The Debtor's remaining assets include  
 17   the sales trailer leased to Royal Marine worth approximately \$273,000, the lease with Royal  
 18   Marine, and the sales office furniture and office equipment, formerly in the sales trailer when it  
 19   housed the Debtor's sales team for the condominium Project, worth approximately  
 20   ~~\$42,000~~42,000.

21                           **B.     LIABILITIES**

22                   The Debtor's only asserted Secured Creditors in this case are Creditors asserting  
 23   that they hold a claim secured by a perfected construction lien asserted under Oregon law or by  
 24   judgment and the county taxing authority. For the reasons set forth at pages 13-14 above, the  
 25   Debtor does not concede that the judgment upon which the asserted Secured Creditors rely is

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valid or that their purported Construction Liens constitute a lien superior in right to the Debtor or its interests. The amount asserted to be perfected Construction Liens under Oregon law or by judgment is approximately \$7.1 million. Multnomah County's personal property and real property tax claim is approximately \$234,000. The Secured Creditors disagree with the Debtor's position regarding their Construction Liens and content that they have valid judgment liens against the Property. The Settlement Parties are settling their claims and disputes under the Settlement Agreement.

As previously explained, there is no other secured debt in this case because the BankFirst debt was eliminated prepetition.

### C. UNSECURED CREDITORS

The Debtor owes approximately \$3 million to unsecured creditors, plus approximately \$10 million to the Debtor's sole member, Mr. DeFrees. The Plan contains two classes of unsecured creditors: Small Unsecured Creditors and General Unsecured Creditors. Small Unsecured Creditors are Creditors holding claims of \$2,000 or less. The total current outstanding amount due to Creditors holding Claims of \$2,000 or less is approximately \$32,000.

### D. ADMINISTRATIVE EXPENSES

The Debtor has retained Farleigh Wada Witt as its general bankruptcy counsel in this case (Docket No. 90) and has ~~filed an application to retain~~retained Dorothy Cofield as its land use counsel (Docket No. ~~94~~105). The Debtor has also retained Obsidian Finance Group, LLC (Docket No. 80) as its financial consultant, and has ~~filed an application to retain~~retained Marcus & Millichap Capital Corporation as its loan broker (Docket No. ~~98~~110). Debtor also hired Spence Powell as its real estate appraiser to prepare an appraisal and to testify at the hearing on Dunn's motion for relief from stay (Docket No. 67). The Debtor anticipates that it will incur approximately \$250,000 in professional fees and expenses through confirmation of the Plan.

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1 **VI. DESCRIPTION OF PLAN OF REORGANIZATION**

2 **A. UNCLASSIFIED CLAIMS**

3 Administrative Expense Claims and Priority Tax Claims are not classified. An  
 4 Administrative Expense Claim is a Claim against the Debtor constituting an expense of  
 5 administration of the Bankruptcy Case allowed under Section 503(b) of the Bankruptcy Code  
 6 including, without limitation, the actual and necessary costs and expenses of preserving the  
 7 estate and operating the Debtor's businesses during the Case, any indebtedness or obligations  
 8 incurred by the Debtor during the pendency of the Case in connection with the rendition of  
 9 services to the Debtor, and compensation for legal and other professional services and  
 10 reimbursement of expenses and statutory fees payable to the United State Trustee.

11 A "Priority Tax Claim" is a Claim of a governmental unit of the kind entitled to  
 12 priority under Section 507(a)(8) of the Bankruptcy Code or that would otherwise be entitled to  
 13 priority but for the Secured status of the Claim. The Debtor owes approximately \$243,000 in  
 14 property taxes. The property taxes will be paid in accordance with the requirements of Section  
 15 1129 of the Bankruptcy Code in ~~equal amortizing~~ payments over a period ending five years from  
 16 the Petition Date.

17 Pursuant to the Plan of Reorganization, Administrative Expense Claims will be  
 18 paid in full on the latter of the Effective Date or the date on which any such Administrative  
 19 Expense Claim becomes an Allowed Claim. However, the Administrative Expense Claims  
 20 representing liabilities incurred in the ordinary course of business (including amounts owed to  
 21 vendors and suppliers that have sold products or furnished services to the Debtor after the  
 22 Petition Date) will be paid in accordance with the written terms and conditions of the particular  
 23 transactions and any other agreements relating thereto. The Debtor will tender a list of such  
 24 ordinary course Administrative Expense Claims at the confirmation hearing.

25 **B. CLASSIFIED CLAIMS**

1                                   **1.       Overall Plan Implementation.**

2                   The Debtor will obtain either ~~an~~ FHA ~~loan~~loans or ~~a~~ conventional ~~loan~~loans to  
3 develop the Property and will pay creditors from a combination of loan proceeds and operating  
4 income.

5                   Initially, the Debtor will obtain a Priming Loan to make parking lot  
6 improvements, to make permit-related payments, to pay professional fees associated with the  
7 bankruptcy case, partition of the Property, loan costs and fees and other site and surveying work.  
8 The general terms of the Priming Loan include: (i) \$500,000, with the possibility of obtaining an  
9 additional \$250,000 upon receipt of a fully-executed commitment letter from a bank or other  
10 financial institution agreement to loan Salpare the funds necessary for the development of  
11 Phase1; (ii) Wall Street prime rate plus 10% floating daily; (iii) \$250,000 to be paid on or before  
12 June 30, 2012 as set forth in the Settlement Agreement; (iv) \$8,000 application fee; (v) loan fee  
13 of 5% upon loan closing; (vi) secured by a first trust deed on the Property; and (vii) release of  
14 trust deed by Priming Loan lender on Phase 1 at closing of Phase 1 FHA Loan. Pursuant to the  
15 Settlement Agreement, the Construction Creditors shall subordinate their liens to the trust deed  
16 of the Priming Loan lender.

17                   ~~If the Debtor obtains FHA financing, it intends to obtain a construction~~As  
18 discussed previously, an FHA Lender has issued a term sheet to the Debtor for an FHA 221(d)(4)  
19 loan for Phase 1 of the construction on the Property ~~in approximately August of 2011~~on or  
20 before June 30, 2012 in the approximate amount of ~~\$2420~~\$2420 million and pay ~~\$3 million to Classes~~  
21 ~~3, 4, 5 and 6 creditors on their Allowed Construction Lien Claims, subject to the outcome of the~~  
22 ~~Dunn Adversary Proceeding, as discussed at Section VI(B)(4) below. The Debtor anticipates~~  
23 ~~completing~~the Discounted Judgment Amount to the Class 2, 3, 4, 5 and 6 Secured Creditors on  
24 their claims in three payments on June 30, 2012, October 31, 2012 and June 30, 2013. The  
25 Debtor will obtain the loan to commence construction of Phase 1 in approximately June of ~~2012.~~

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~~At that point,~~ 2012 with funding provided by the FHA Lender. By October 31, 2012, the Debtor will refinance the Marina and ~~pay \$3 million to Classes 3, 4, 5 and 6 creditors on their Allowed Construction Lien Claims, subject to the outcome of the Dunn Adversary Proceeding, as discussed at Section VI(B)(4) below infra~~ make the second installment payment to the Secured Creditors as well as the first payment to Multnomah County, the first payment to General Unsecured Creditors and the final payment to the Small Unsecured Creditors. The Debtor intends to obtain financing for Phase 2 of the construction on the Property in approximately June of 2013, at which time the Debtor will pay ~~Class 3, 4, 5 and 6 Claimants~~ the Secured Creditors their final payment pursuant to the Settlement Agreement. The Debtor plans to pay Small Unsecured Creditors and General Unsecured Creditors from ~~net operating income or loan proceeds~~ Net Income.

The Debtor proposes to implement this Plan as set forth in the Plan projections attached hereto as Exhibit 5.

## **2. Class 1 (Other Priority Claims).**

Class 1 is unimpaired. Each holder of an Allowed Class 1 Claim will be paid in full in Cash the amount of its Allowed Class 1 Claim, including all interest, costs, fees and charges provided for under any agreement under which such Claim arose or is otherwise allowed by law, on the latter of (a) the Effective Date or (b) the date on which such Claim becomes Allowed, unless such holder shall agree or has agreed to a different treatment of such Claim (including any different treatment that may be provided for in any documentation, agreement, contract, statute, law or regulation creating and governing such Claim. The Debtor is not aware of the existence of any Other Priority Claims.

## **3. Class ~~3~~2 (City of Portland Secured Claim).**

Class 2 consists of the Claim asserted by the City of Portland under ORS 223, the city charter of Portland and the Portland City Code, as set forth in the Dunn Action judgment in

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the amount of \$152,028.81 as a Secured Claim. The holder of an Allowed Secured Class 2 Claim will be paid as set forth ~~in full in Cash the amount of its Allowed Class 2 Claim, on the latter of the closing of the loan the Debtor will obtain for the development of Phase 1 or September 30, 2011.~~ the Settlement Agreement its share of the Discounted Judgment Amount as follows: 40% on or before June 30, 2012; 40% on or before October 31, 2012 and the remaining 20% on or before June 30, 2013.

#### 4. Class 3 through 56 (Construction Liens).

Classes 3 through 6 are impaired and consist of Claims asserted by: Dunn (Class 3), TKS (Class 4), BMI (Class 5) and Myhre (Class 6). Each Creditor holding a Class 3, 4, 5 or 6 Allowed Claim secured by a perfected construction lien will retain its lien with the same priority such lien had on the Petition Date, except as set forth herein at Section 6.3 of ~~this~~ the Plan. The Allowed Claims in Classes 3, 4, 5 and 6 will be paid ~~in full~~ the Discounted Judgment Amount, together with interest accruing from and after the Effective Date at the rate of 3.25% per annum from the proceeds of the ~~refinancing~~ financing of the Property, consistent with the terms of the Settlement Agreement. The first payment to Classes 3, 4, 5 and 6 ~~on their Allowed Construction Lien Claims (subject to the outcome of the Dunn Adversary Proceeding), of 40% of the Discounted Judgment Amount~~ will occur on the ~~later of the~~ closing of the loan Debtor will obtain to develop Phase 1 or ~~September 30, 2011, and will be in the approximate amount of \$3 million. In June~~ June 30, 2012, as set forth in the Settlement Agreement. On or before October 31, 2012, the Debtor anticipates refinancing the Marina and will pay approximately \$3 million at the later of the closing of that loan or August 30, 2012 to the Allowed Construction Lien Claims. 40% of the Discounted Judgment Amount to Classes 3, 4, 5 and 6 as set forth in the Settlement Agreement. The Debtor intends to obtain financing to develop Phase 2 ~~in~~ approximately on or before June 30, 2013 and will pay the balance of the ~~Allowed Construction~~

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~~Lien Claims on the later of the closing of that loan or June 30, 2013.<sup>5</sup> The Multnomah County Circuit Court (the "State Court") granted Classes 3, 4, 5 and 6 a Limited Judgment against the Debtor in the Dunn Action; however, that Limited Judgment was entered in September of 2009 *nunc pro tunc* to April 21, 2009, thus invalidly cutting off parties' appeal rights. Moreover, when the State Court entered the Limited Judgment, the case had already been removed to federal court, thus eliminating the State Court's jurisdiction to enter the Limited Judgment. Following the transfer of the Dunn Action back to the State Court, an Order Reaffirming the Limited Judgment was signed and entered on January 22, 2010, but no separate Limited Judgment was entered on that date and the Order Reaffirming the Limited Judgment did not correct the inappropriate *nunc pro tunc* entry that cut off parties' appeal rights. The Debtor contests the validity of the Limited Judgment in favor of the Class 3, 4, 5 and 6 Claimants in the Dunn Adversary Proceeding pending before the Bankruptcy Court, in which the Debtor seeks a declaratory judgment that: (i) the Limited Judgment is void; (ii) the Debtor is equitably subrogated to the rights of BankFirst under the BankFirst DOT; (iii) pursuant to ORS 87.025(2), the Class 3, 4, 5 and 6 Claimants are entitled to foreclose their interest in and remove the Improvements they created on the Property, but are not entitled to foreclose their interest in the Property ahead of the BankFirst DOT; and (iv) any judgment of foreclosure entered in the future (in the event the automatic stay were lifted to allow entry of the judgment) shall reflect: (a) the BankFirst DOT's superior position with respect to the Land; (b) any foreclosure sale held by Dunn, TKS, and/or Myhre shall include only the Improvements, and that any foreclosure sale of the Land by those parties shall be subject to the BankFirst DOT; and (c) the purchaser at any~~

<sup>5</sup> If the Debtor obtains conventional financing, the Debtor intends to proceed the same way as it would if it were obtaining FHA financing, with the following differences: (1) it will pay approximately \$1 million instead of \$3 million upon the initial financing anticipated to be in September of 2011 to Class 3, 4, 5 and 6 Claimants on their Allowed Construction Lien Claims, subject to the outcome of the Dunn Adversary Proceeding; and (2) it will obtain permanent financing for Phase 1 and pay approximately \$2 million to Class 3, 4, 5 and 6 Claimants on their Allowed Construction Lien Claims on the later of the closing of that loan or June 13, 2013, along with the payment from the financing for Phase 2 as discussed above.

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~~foreclosure sale held with respect to the Improvements shall be required to remove the Improvements within 30 days, subject to the terms and conditions of ORS 87.035(3). Should the Debtor prevail in the Dunn Adversary Proceeding, then the Class 3, 4, 5 and 6 Allowed Claims will be paid an amount equivalent to the fair market value of the Improvements that each of the Claimants made to the Property from the refinancing of the Property by the Debtor, with interest at the rate of 3.25% per annum. Thereafter, the Class 3, 4, 5 and 6 Claimants will retain their liens and will be treated as Secured Claims only to the extent of any value securing the lien after satisfaction of the BankFirst DOT. To the extent the value of the Property is insufficient to pay such lien, the holder will have a Small Unsecured Claim or a General Unsecured Claim, as appropriate. The Unsecured Claim will be the difference between the Claim on the Petition Date and the payment the Debtor makes to the Claimant based upon the fair market value of their respective Improvements from the refinance of the Property. Any disputes regarding the allowance of a Class 3, 4, 5 and 6 Claim may be determined in the Dunn Adversary Proceeding or by the claims objection process.~~ Discounted Judgment Amount to Classes 3, 4, 5 and 6 as set forth in the Settlement Agreement. Debtor shall deliver a Bargain and Sale Deed to the Property (the "Deed") (free and clear of all liens), except those permitted under the Plan and the Settlement Agreement, conveying the Property to Dunn to Judge Hogan to be held in trust for the benefit of the Construction Creditors within five (5) business days of the Effective Date. After each payment referenced herein, Debtor shall immediately deliver to Judge Hogan a new deed for the portion(s) of the Property that remain as collateral for Debtor's payment obligations to the Construction Creditors.

##### **5. Class 7 (County Secured Claim for Property Taxes).**

Class 7 is unimpaired. The holder of the Class 7 Claim will retain its security interest with the same priority to which it is entitled by law. The Allowed Class 7 Claimant shall be paid the full amount of its Secured Claim as permitted by 11 USC §1129(a)(9)(D) in full from

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financing of the Property or ~~net operating income~~ Net Income, but not later than five (5) years after the Petition Date.

**6. Class 8 (Small Unsecured Claims).**

Class 8 is impaired. Each holder of a Class 8 Claim will be paid in Cash an amount equal to 25% of their Allowed Claim ~~within 60 days of the Effective Date of the Plan on~~ or before October 31, 2012 or 30 days of the date their Claim becomes an Allowed Claim, whichever is later. Thereafter, each holder of a Class 8 Claim will be paid in Cash an amount equal to 75% of their Allowed Claim on or before ~~October 31, 2011.~~ June 30, 2013. The total costs of payment to current Small Unsecured Creditors will be approximately \$31,000.

**7. Class 9 (General Unsecured Claims).**

Class 9 is impaired. Each holder of a Class 9 Claim shall be paid by receiving a Pro Rata share of 30% of the Net ~~Operating~~ Income generated by the Reorganized Debtor for each calendar quarter from after ~~September 30, 2011 for five (5) years. Additionally, any~~ June 30, 2012 through December 31, 2017, so long as the Debtor has amounts in excess of \$~~23.5 million~~ 500,000 in ending cash balances ~~as of October 31, 2016, if any, shall be paid to Class 9 Allowed Claims to the extent necessary to pay such Claims, if possible.~~ General Unsecured Claims total approximately \$2.2 million, plus approximately \$10.9 million to General Unsecured Claims owing to Michael DeFrees, plus any Deficiency Claims of Secured Claims. Mr. DeFrees has agreed to subordinate payments to him on his General Unsecured Claim and he will be treated as a Class 9 Claimant.

**8. Class 10 (Subordinated Claims).**

Class 10 is impaired. Holders of subordinated claims will be paid a Pro Rata share of all remaining Unsecured proceeds after Holders of allowed Class 9 Claims have been paid in full.

**9. Class 11 (Interests).**

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Class 11 is impaired. The holder of the Class 11 Claims ~~is~~are the holders of all equity interests in the Debtor. ~~All~~As a result of the Settlement Agreement, the owners of Harbor will transfer their membership interests in Harbor to Salpare. The interests of Salpare owned by Harbor will then be cancelled. All remaining equity interests will be retained by Mr. DeFrees in exchange for the subordination of his \$10.9 million General Unsecured Claim, ~~the interests in the Reorganized Debtor will be issued to Mr. DeFrees.~~

### C. EXECUTORY CONTRACTS AND UNEXPIRED LEASES

The Bankruptcy Code gives Debtor the right, after commencement of their Chapter 11 cases, subject to the approval of the Bankruptcy Court, to assume or reject executory contracts and unexpired leases. Generally, an “executory contract” is a contract under which material performance (other than payment of money) is still due by each party. The Plan provides for assumption of all executory contracts and leases.

If an executory contract or unexpired lease is or has been rejected, the Creditor may file a Proof of Claim for damages resulting from such rejection. The Plan provides that a Proof of Claim with respect to any such Claim must be Filed no later than 30 days after approval of the Bankruptcy Code of the rejection of the relevant executory contract or unexpired lease or 30 days after the Effective Date, whichever is sooner. Any such Claim shall constitute an Unsecured Claim to the extent that such Claim is finally treated as an Allowed Claim. To the extent the Debtor rejects an unexpired lease of nonresidential real property, the Claim for damages resulting from such rejection will be limited to the amount allowed under the Bankruptcy Code.

Upon assumption of an executory contract or unexpired lease, the Debtor must cure or provide adequate assurance of prompt cure of any monetary defaults. The Plan provides that the Reorganized Debtor will cure all defaults, if any, in the ordinary course of business and will cure any monetary defaults, if any, promptly. All assumed executory contracts and leases

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will be automatically assigned to the Reorganized Debtor as of the Effective Date. The Debtor assumed the leases and executory contracts listed on Exhibit 6.

#### **D. EFFECT OF CONFIRMATION**

##### **1. DISCHARGE**

The treatment of, and consideration received by, holders of Allowed Claims and Allowed Interests pursuant to the Plan will be in full satisfaction, release and discharge of their respective Claims against or interests in the Debtor. Confirmation Orders shall discharge the Debtor from any liability that arose before the Effective Date as provided in Sections 524 and 1141 of the Bankruptcy Code, and any debt and liability of a kind specified in Sections 502(g), 502(h) or 502(i) of the Bankruptcy Code, whether or not: (a) a Proof of Claim based on such debt or liability is filed or deemed filed under Section 501 of the Bankruptcy Code; (b) a Claim based on such debt or liability is Allowed; or (c) the holder of the Claim based on such debt or liability has accepted the Plan.

##### **2. REVESTING, OPERATION OF BUSINESS**

All property of the estates shall revest in Reorganized Debtor on the Effective Date free and clear of all rights, claims, liens charges, encumbrances and interests, except as otherwise provided in the Plan.

##### **3. INJUNCTION**

Except as otherwise expressly provided in the Plan, all persons who have held, hold or may hold Claims, or who may have held, hold or may hold any Interest, are permanently enjoined from and after the Effective Date from (a) commencing or continuing in any manner any action or other proceedings of any kind with respect to any Claims or Interests against Reorganized Debtor; (b) enforcing, attaching, collecting or recovering by any manner or any means any judgment, award, decree or order against Reorganized Debtor; (c) creating, perfecting or enforcing any encumbrances of any kind against Reorganized Debtor with respect to any such

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1 Claim except as specifically set forth in the Plan; (d) asserting any setoff, right of subrogation or  
 2 recoupment of any kind against any obligation due to the Debtor, Reorganized Debtor or their  
 3 property; and (e) proceeding in any manner in any place whatsoever that does not conform to,  
 4 does not comply with, or is inconsistent with the provisions of the Plan or the order confirming  
 5 the Plan.

#### 6 **4. MODIFICATION OF THE PLAN; REVOCATION OR** 7 **WITHDRAWAL OF THE PLAN**

8 Subject to Section 1127 of the Bankruptcy Code, the Debtor reserves the right to  
 9 alter, amend or modify the Plan before its substantial consummation so long as the treatment of  
 10 holders of Claims and Interests under the Plan are not adversely affected.

#### 11 **5. RETENTION OF JURISDICTION**

12 Notwithstanding the entry of the Confirmation Order on the Effective Date having  
 13 occurred, the Bankruptcy Court shall retain exclusive jurisdiction over all matters arising out of  
 14 or relating to the Chapter 11 Case, including, but not limited to, the following matters: (a) to  
 15 hear and determine any pending applications for the rejection of executory contracts or  
 16 unexpired leases, and the allowance of Claims resulting therefrom; (b) to determine any  
 17 adversary proceedings, applications, contested matters or other litigative matters pending on the  
 18 Effective Date or Filed prior to the closing of the case; (c) to ensure that distributions to holders  
 19 of Allowed Claims are accomplished; (d) to hear and determine objections to or requests for  
 20 estimations of Claims, including any objections to the classification of any Claim, and to allow,  
 21 disallow and/or estimate any Claim in whole or in part; (e) to enter and implement such orders as  
 22 may be appropriate in the event the Confirmation Order is for any reason stayed, revoked,  
 23 modified or vacated; (f) to issue any appropriate orders in aid of execution of the Plan or to  
 24 enforce the Confirmation Order and/or the discharge, or the effect of such discharge, provided to  
 25 the Debtor; (g) to hear and determine any applications to modify the Plan, to cure any defect or  
 26 omission or to reconcile any inconsistency in the Plan or in any order of the Bankruptcy Court,

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including, without limitation, the Confirmation Order; (h) to hear and determine all applications for compensation and reimbursement of expenses of professionals or members of the Creditors Committee under the Bankruptcy Code; (i) to hear and determine disputes arising in connection with the interpretation, implementation and enforcement of the Plan; (j) to hear and determine other issues presented or arising under the Plan; (k) to hear and determine any other matters related hereto and not inconsistent with Chapter 11 of the Bankruptcy Code; and (l) to enter a final decree closing the Chapter 11 Case.

#### 6. UNITED STATES TRUSTEE FEES

Reorganized Debtor shall be responsible for timely payment of fees incurred pursuant to 28 USC § 1930(a)(6) until the case is closed, converted or dismissed. After confirmation, Reorganized Debtor shall serve on the United States Trustee a monthly financial report for each month, or portion thereof, that the case remains open. The monthly financial report shall include a statement of all disbursements made during the course of the month, whether or not pursuant to the Plan.

#### 7. AVOIDANCE ACTIONS.

The Debtor has not done an analysis of possible preference or fraudulent transfer actions. The Debtor has not budgeted Professional Fees to pursue preference claims, but has also not budgeted for any recovery. If any such claims exist, the Professional Fees would presumably be covered by any recoveries. The Debtor will complete a preference analysis before the hearing date on Confirmation. The Plan preserves all avoidance actions to the extent any exist.

### VII. LIQUIDATION ANALYSIS

A Plan of Reorganization cannot be confirmed unless the Bankruptcy Court finds that the Plan is in the “best interest of creditors” of holders of claims against, and interests in, the debtor subject to such plan. The best interest test is satisfied if the plan provides each dissenting or non-voting member of each impaired Class with a recovery not less than the recover such

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1 member would receive if the debtor was liquidated in a hypothetical case under Chapter 7 of the  
 2 Bankruptcy Code by a Chapter 7 Trustee. The Debtor believes that the holders of impaired  
 3 Claims will receive more than they would receive under a Chapter 7 liquidation. In applying the  
 4 “best interest” test, the Bankruptcy Court would ascertain the hypothetical recovery in a Chapter  
 5 7 proceeding to Secured Creditors, priority claimants, general Unsecured Creditors and equity  
 6 interest holders. The hypothetical Chapter 7 recoveries would then be compared with the  
 7 distribution offered to each Class of Claims or Interests under the Plan to determine that the Plan  
 8 satisfied the “best interest” test set forth in the Bankruptcy Code.

9 A copy of the Debtor’s tabulation liquidation analysis is attached hereto as Exhibit ~~4~~7. The  
 10 liquidation table shows that upon a liquidation of the Debtor, there would be no funds available  
 11 for distribution to Unsecured Creditors.

## 12 **VIII. CERTAIN U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE** 13 **PLAN**

14 CIRCULAR 230 DISCLAIMER: TO ENSURE COMPLIANCE WITH  
 15 REQUIREMENTS IMPOSED BY THE INTERNAL REVENUE SERVICE, WE INFORM  
 16 YOU THAT (A) ANY U.S. FEDERAL TAX ADVICE CONTAINED IN THIS  
 17 COMMUNICATION (INCLUDING ANY ATTACHMENTS) IS NOT INTENDED OR  
 18 WRITTEN TO BE USED OR RELIED UPON, AND CANNOT BE USED OR RELIED  
 19 UPON, FOR THE PURPOSE OF (1) AVOIDING TAX-RELATED PENALTIES UNDER THE  
 20 INTERNAL REVENUE CODE OF 1986, AS AMENDED, OR (2) PROMOTING,  
 21 MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY TRANSACTION OR  
 22 TAX MATTER(S) ADDRESSED HEREIN, AND (B) THIS DISCUSSION WAS WRITTEN  
 23 IN CONNECTION WITH DEBTOR SOLICITING ACCEPTANCES OF THE PLAN  
 24 THROUGH THIS DISCLOSURE STATEMENT.

### 25 **A. GENERAL TAX CONSIDERATIONS**

1 The following discussion is a summary of certain material federal income tax  
 2 consequences expected to result from the consummation of the Plan. This discussion is for  
 3 general information purposes only, and should not be relied upon for purposes of determining the  
 4 specific tax consequences of the Plan with respect to a particular holder of an Allowed Claim or  
 5 equity interest. This discussion does not purport to be a complete analysis or listing of all  
 6 potential tax considerations. This discussion does not address aspects of federal income taxation  
 7 that may be relevant to a particular holder of an Allowed Claim subject to special treatment  
 8 under federal income tax laws (such as foreign taxpayers, broker-dealers, banks, thrifts,  
 9 insurance companies, financial institutions, regulated investment companies, real estate  
 10 investment trusts and pension plans, and other tax-exempt investors), and does not discuss any  
 11 aspects of state, local or foreign tax laws. Furthermore, this summary does not address federal  
 12 taxes other than income taxes.

13 This discussion is based on existing provisions of the Internal Revenue Code of  
 14 1986, as amended (the "IRC"), existing and proposed Treasury Regulations promulgated  
 15 thereunder, and current administrative rulings and court decisions. Legislative, judicial or  
 16 administrative changes or interpretations enacted or promulgated after the date hereof could alter  
 17 or modify the discussion set forth below with respect to federal income tax consequences of the  
 18 Plan. Any such changes or interpretations may be retroactive and could significantly affect the  
 19 federal income tax consequences of the Plan. No ruling has been requested or obtained from the  
 20 Internal Revenue Service (the "IRS") with respect to any tax aspects of the Plan and no opinion  
 21 of counsel has been sought or obtained with respect thereto. This discussion is not binding on  
 22 the IRS or the courts and no assurance can be given that the IRS will not assert, or that a court  
 23 will not sustain, a different position than any position discussed herein. No representations or  
 24 assurances are being made to the holders of Allowed Claims or equity interests with respect to  
 25 the federal income tax consequences described herein.

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Accordingly, the following summary of certain federal income tax consequences of the Plan is for informational purposes only and is not a substitute for careful tax planning or advice based upon the individual circumstances pertaining to a particular holder of an Allowed Claim or an equity interest. Each holder of an Allowed Claim or an equity interests is strongly urged to consult with its own tax advisors regarding the federal, state, local, foreign and other tax consequences of the Plan.

Any discussion of federal tax issues set forth in this Disclosure Statement was written solely in connection with the confirmation of the Plan to which the transactions described in this Disclosure Statement are ancillary. Such discussion is not intended or written to be legal or tax advice to any person and is not intended or written to be used, and cannot be used, by any person for the purpose of avoiding any federal tax penalties that may be imposed on such person. Each holder of an Allowed Claim or equity interest should seek advice based on its particular circumstances from an independent tax advisor.

## **B. FEDERAL INCOME TAX CONSEQUENCES TO DEBTORS**

### **1. IN GENERAL**

The Debtor is a limited liability company and, thus, is a pass-through entity for both federal and state income tax purposes. As such, the Debtor is not itself subject to federal income tax. Instead, the Debtor's sole member is required to include on his personal income tax return the income, gain, loss and deduction recognized by the Debtor. Accordingly, it is unlikely that there will be any direct federal income tax liability at the Debtor's entity level.

### **2. CANCELLATION OF INDEBTEDNESS INCOME**

Under the IRC, a taxpayer generally will recognize cancellation of debt income ("COD Income") upon satisfaction of its outstanding indebtedness for consideration less than the amount of such indebtedness. The amount of COD Income, in general, is the excess of (a) the adjusted issue price of the indebtedness (in most cases, the amount the debtor received on

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1 incurring the obligation, with certain adjustments) satisfied, over (b) the sum of the amount of  
 2 Cash paid and the fair market value of any new consideration given in satisfaction of the  
 3 indebtedness.

4 However, IRS Section 108(a) provides an exclusion from gross income for COD  
 5 income if certain requirements are met. Section 108(a) provides an exclusion commonly referred  
 6 to as the "Bankruptcy Exception," where a taxpayer is in bankruptcy and the discharge is  
 7 granted, or is effected, pursuant to a plan approved by the bankruptcy court. In the case of an  
 8 entity taxable as a corporation, eligibility for the Bankruptcy Exception is determined at the  
 9 corporate level. If the Bankruptcy Exception applies (with the effect that the taxpayer may  
 10 exclude its COD Income from its gross income), the taxpayer is required, under IRS Section  
 11 108(b), to reduce certain of its tax attributes by the amount of COD Income excluded from gross  
 12 income pursuant to the Bankruptcy Exception. The attributes of the taxpayer that are reduced  
 13 include any net operation loss carryovers from prior years, general business and minimum tax  
 14 credit carryforwards, capital loss carryforwards, the basis of the taxpayer's assets and foreign tax  
 15 credit tax carryforwards. In the limited liability company context, the reduction in the basis of  
 16 assets is most important. However, a special rule can also require a reduction in certain losses to  
 17 be passed through to members of limited liability companies.

## 18 C. FEDERAL INCOME TAX CONSEQUENCES TO THE HOLDERS 19 OF AN ALLOWED CLAIM

### 20 1. SMALL UNSECURED CREDITOR CLAIMS

21 In accordance with the Plan, the debt owed by the Debtor to each holder of a  
 22 Small Unsecured Claim will be satisfied by a payment of Cash in an amount equal to 100% of  
 23 such Claim. In general, the amount received by each holder of a Small Unsecured Claim is  
 24 treated as an amount received in exchange for the satisfied debt, and each such holder will  
 25 recognized taxable gain or loss equal to the amount received less the holder's tax basis in the  
 26 Claim. Any gain or loss recognized will be long-term or short-term capital gain or loss or

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ordinary income or loss, depending upon factors specific to each holder of a Small Unsecured Claim, including but not limited to: (i) whether the Claim (or a portion thereof) is attributable to principal or interest; (ii) the origin of the Claim; (iii) whether the holder of the Claim reports income on the accrual or cash basis method; and (iv) whether the holder of the Claim has taken a bad debt deduction or otherwise recognized a loss with respect to the Claim.

## 2. GENERAL UNSECURED CREDITOR CLAIMS

In accordance with the Plan, the debt owed by the Debtor to each holder of a General Unsecured Claim will be adjusted so that each General Unsecured Creditor will be entitled to a Pro Rata share of 30% of the Net ~~Operating~~ Income generated by the ~~Reorganzied~~Reorganized Debtor ~~for five years through December 31, 2017.~~ If this adjustment is considered significant, each such holder will recognize taxable gain or loss equal to the difference between the fair market value of the obligation as adjusted and the holder's adjusted basis in the original debt. It may be difficult to place a value on the obligation as adjusted, but gain may nevertheless be recognized. The character and amount of such taxable gain or loss will be determined based on factors specific to each holder of a Claim, as discussed above with respect to Small Unsecured Claims.

## 3. OREGON CONSTRUCTION LIEN CREDITOR CLAIMS

In accordance with the Plan, the debt owed by the Debtor to each holder of an Allowed Construction Lien Claim will be restructured. If the modification to the debt is "significant," as such term is defined in the applicable Treasury Regulations, the restructured debt will be treated as received by such holder in a deemed taxable exchange of the underlying debt pursuant to IRC Section 1001.

With respect to a deemed taxable exchange, a holder of an Allowed Construction Lien Claim will generally recognize gain or loss in connection with the exchange if the holder's adjusted tax basis in the old debt does not equal the issue price of the modified debt. If the issue

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price of the modified debt is greater than the holder's adjusted tax basis in the debt, the holder will recognize taxable income as a result of the deemed exchange. Since each modified debt will have a principal amount equal to its corresponding old debt, and each modified debt will have adequate stated interest, a holder of an Allowed Construction Lien Claim generally should not recognize any gain or loss on a deemed taxable exchange of such debt unless the tax basis in the debt is different from the issue price of the modified debt. The character and amount of any taxable gain or loss will be determined based on factors specific to each holder of a Claim, as discussed above with respect to Small Unsecured Claims.

The principal amount of certain restructured debt may include accrued but unpaid interest. A holder of an Allowed Construction Lien Claim not previously required to include in its taxable income any accrued but unpaid interest on such Claim may be treated as receiving taxable interest to the extent the modified debt received is allocable to such accrued but unpaid interest.

#### **D. CONSEQUENCES TO HOLDERS OF EQUITY INTERESTS**

Pursuant to the Plan, all of the currently outstanding membership interests of the Debtor shall be deemed cancelled and shall be of no further force and effect, whether surrendered for cancellation or otherwise, and there shall be no distribution with respect to such shares. The IRS may assert that the COD Income discussed above is not subject to the Bankruptcy Exception because, in the case of an entity taxed as a partnership, the exclusions of Section 108(a) are determined in relation to the members' situations, not the situation of the entity that realizes the COD Income. If this result obtains, a member may have to include such COD Income in gross income, and this inclusion would increase his, her or its basis in the membership interests. Moreover, upon extinguishment of the member's interests in the Debtor, the member may be deemed to receive a distribution equal to the Debtor's liabilities, which reduces the member's basis. If the reduction in liabilities exceeds basis, the member would

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1 realize gain. If the member has an unrecovered basis at the time of extinguishment of his  
 2 interests, he may be able to claim a loss, which the IRS is likely to characterize as capital rather  
 3 than ordinary. To the extent that that sole member of the Debtor invests additional monies in the  
 4 Debtor, this should created basis in the new membership interests to be issued by the Debtor.

#### 5 **E. INFORMATION REPORTING BACKUP WITHHOLDING**

6 Certain payments, including the payments with respect to Claims pursuant to the  
 7 Plan, are generally subject to information reporting by the payor to the IRS. Moreover, under  
 8 certain circumstances, a holder of a Claim may be subject to “backup withholding” with respect  
 9 to payments made pursuant to the Plan, unless such holder either (i) comes within certain exempt  
 10 categories (which generally include corporations) and, when required, demonstrates this fact, or  
 11 (ii) provides a correct United States taxpayer identification number and certified under penalty of  
 12 perjury that the holder is a United States person, the taxpayer identification is correct and that the  
 13 taxpayer is not subject to backup withholding because of a failure to report all dividend and  
 14 interest income. Backup withholding is not an additional tax. Amounts withheld under the  
 15 backup withholding rules may be credited against the holder’s United States federal income tax  
 16 liability, and the holder may obtain a refund of any excess amounts withheld under the backup  
 17 withholding rules by filing an appropriate claim for refund with the IRS.

#### 18 **F. IMPORTANCE OF OBTAINING PROFESSIONAL TAX ASSISTANCE**

19  
 20 THE FOREGOING DISCUSSION IS INTENDED ONLY AS A SUMMARY  
 21 OF CERTAIN U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE PLAN AND IS  
 22 NOT A SUBSTITUTE FOR CAREFUL TAX PLANNING WITH A TAX PROFESSIONAL.  
 23 THE ABOVE DISCUSSION IS FOR INFORMATIONAL PURPOSES ONLY AND IS NOT  
 24 TAX ADVICE. THE TAX CONSEQUENCES ARE IN MANY CASES UNCERTAIN AND  
 25 MAY VARY DEPENDING ON THE PARTICULAR SITUATION OF A HOLDER OF AN

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1 ALLOWED CLAIM, OR ANY EQUITY INTEREST HOLDER'S PARTICULAR  
 2 CIRCUMSTANCES. ACCORDINGLY, EACH HOLDER OF AN ALLOWED CLAIM AND  
 3 EACH EQUITY INTEREST HOLDER IS URGED TO CONSULT ITS TAX ADVISOR  
 4 ABOUT THE FEDERAL, STATE, LOCAL AND APPLICABLE FOREIGN INCOME AND  
 5 OTHER TAX CONSEQUENCES OF THE PLAN.

## 6 **IX. ACCEPTANCE AND CONFIRMATION OF THE PLAN**

### 7 **A. CONFIRMATION HEARING**

8 The Bankruptcy Court has scheduled a hearing on confirmation of the Plan on  
 9 \_\_\_\_\_, ~~2010~~2011 at \_\_\_\_\_. The hearing will be held at the United States Bankruptcy Court  
 10 for the District of Oregon, Courtroom No. 4, 1001 SW Fifth Avenue, Portland, Oregon 97204,  
 11 before the Honorable Trish M. Brown, United State Bankruptcy Judge. At that hearing, the  
 12 Bankruptcy Court will consider whether the Plan satisfied the various requirements of the  
 13 Bankruptcy Code, including whether it is feasible, and whether it is in the best interest of  
 14 Creditors and Interest Holders of the the Debtor. Debtor will submit a report to the Bankruptcy  
 15 Court at that time concerning the votes for acceptance or rejection of the Plan by the parties  
 16 entitled to vote thereon. Any objection to confirmation of the Plan must be timely filed as stated  
 17 in Section II.E. above.

### 18 **B. REQUIREMENTS OF CONFIRMATION**

19 At the hearing on confirmation, the Bankruptcy Court will determine whether the  
 20 provisions of Section 1129 of the Bankruptcy Code have been satisfied. If all of the provisions  
 21 of Section 1129 are met, the Bankruptcy Court may enter an order confirming the Plan. The  
 22 Debtor believes the Plan satisfies all of the requirements of Chapter 11 of the Bankruptcy Code,  
 23 that it has complied or will have complied with all of the requirements of Chapter 11, and that it  
 24 has been proposed and is made in good faith.

### 25 **C. FEASIBILITY**

Attached as Exhibit 5 is Debtor's projected income and Net-~~Operating~~ Income and other distribution projections. The projections support the treatment of claims set forth in Section VI above.

#### **D. RISK FACTORS**

There are a number of risks associated with the Debtor's proposed Plan. Each Creditor should carefully consider those risks in evaluating its vote on the Debtor's Plan. All of the risks associated with the Debtor's Plan are too numerous to identify. However, a few of those risks are set forth below.

##### **1. GENERAL FINANCIAL MARKET CONDITIONS**

The recent disruption with numerous major financial institutions and the resulting crisis in the financial markets has rippled through the economy, and has impacted the condominium and residential housing market in particular. While the ultimate effect of this crisis on the residential housing market is yet unclear, it is possible that this financial market will adversely affect the ability of the Debtor to develop the Property as set forth in this Plan.

##### **2. PROJECTED FINANCIAL RESULTS**

The Debtor projected financial results reflect management's best estimate of the Reorganized Debtor's future financial performance based on currently known facts and hypothetical assumptions about, among other matters, the timing, confirmation and consummation of the Plan in accordance with its terms, the anticipated future performance of the Reorganized Debtor, residential housing industry performance, and general business and economic conditions. Many of these factors are beyond the control of the Reorganized Debtor. As a consequence, the actual financial results may differ significantly from the projections. Specifically, the Reorganized Debtor may not be able to meet the projected financial results or achieve the revenue or cash flow that it has assumed in projecting future business prospects.

##### **3. DEPENDENCE ON SUBCONTRACTORS**

The development of the Project depends on construction work done by subcontractors. The Reorganized Debtor's business model relies heavily upon maintaining its existing relationship with its core group of highly skilled and experienced subcontractors. As a result, insufficient availability of, or unsatisfactory performance by these third-party subcontractors could have a material adverse affect on the Debtor's business.

#### 4. CLAIM AMOUNTS

The claims estimates set forth in this Disclosure Statement are based on various assumptions. The actual Allowed Claim amounts may differ significantly from these estimates should one or more of Debtor's underlying assumptions prove to be incorrect. Such differences may materially and adversely affect the percentage recovery to holders of such Claims under the Plan.

#### E. CRAM DOWN

As discussed previously, a Court may confirm a Plan, even if it is not accepted by all impaired classes, if the Plan has been accepted by at least one impaired class of claims and the Plan meets the cram down requirements set forth in Section 1129(b) of the Bankruptcy Code. In the event that any impaired Class of Claims does not accept the Plan, the Debtor hereby requests that the Bankruptcy Court confirm the Plan in accordance with Section 1129(b) of the Bankruptcy Code or otherwise permit the Debtor to modify the Plan.

The Debtor believes the Plan does not violate the absolute priority rule of the Bankruptcy Code. 11 USC §1129(b)(2)(B)(ii), commonly referred to as the absolute priority rule, provides that with respect to a class of unsecured claims, the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property unless the plan provides that each holder of a claim receives or retains on account of such claim property of a value, as of the Effective Date of the plan, equal to the Allowed amount of such claim.

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1 **F. ALTERNATIVES TO CONFIRMATION OF THE PLAN**

2 If a Plan is not confirmed, the Debtor or another party in interest may attempt to  
3 formulate or propose a different Plan or Plans of Reorganization. Such Plans might involve a  
4 reorganization and continuation of the Debtor's business, the sale of the Property or a portion  
5 thereof, an orderly liquidation of the Debtor's assets or any combination thereof. If no Plan of  
6 Reorganization is determined by the Bankruptcy Court to be confirmable, the Chapter 11 case  
7 may be converted to a liquidation proceeding under Chapter 7 of the Bankruptcy Code.

8 In a liquidation, a Chapter 7 Trustee would be appointed with the purpose of liquidating the  
9 assets of the Debtor. Typically, in a liquidation, assets are sold for less than their going concern  
10 value and, accordingly, the return to Creditors and Interest holders is less than the return in a  
11 reorganization, which derives the value to be distributed in a Plan from the business as a going  
12 concern. Proceeds from liquidation would be distributed to Creditors and Interest holders of the  
13 Debtor in accordance with the priorities set forth in the Bankruptcy Code.

14 The Debtor believes that there is no currently available alternative that would  
15 offer holders of Claims and Interests in the Debtor greater than the Plan and urges all parties  
16 entitled to vote on the Plan to vote to accept the Plan.

17 **X. CONCLUSION**

18 Please read this Disclosure Statement and the Plan carefully. After reviewing all  
19 the information and making an informed decision, please vote by using the enclosed ballot.

20 Dated: ~~September 7, 2010~~ April 8, 2011.

21 Respectfully submitted,

22 SALPARE BAY, LLC

23 By: ITS MANAGER, COLUMBIA RIM  
24 CORPORATION, a Washington corporation

25 By: /s/ Michael J. DeFrees  
Michael J. DeFrees, President

26 Presented by:

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6  
7 IN THE UNITED STATES BANKRUPTCY COURT  
8 FOR THE DISTRICT OF OREGON

9 In re

10 Salpare Bay, LLC,

11 Debtor.  
12  
13

Case No. 10-35333-tmb11

DEBTOR'S FIRST AMENDED CHAPTER 11  
DISCLOSURE STATEMENT (APRIL 8, 2011)

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1                   **I. INTRODUCTION AND SUMMARY OF PLAN**

2                   **A. INTRODUCTION**

3                   On June 7, 2010 (the "Petition Date"), Salpare Bay, LLC ("Debtor" or "Salpare")  
4                   filed a voluntary petition under chapter 11 of Title 11 of the United States Code (the  
5                   "Bankruptcy Code"). The Debtor is seeking acceptance of Debtor's Plan of Reorganization (the  
6                   "Plan") by the creditors of the Debtor's estate. This Disclosure Statement (the "Disclosure  
7                   Statement") describes:

- 8                   • Historical information regarding the Debtor and the events leading to its  
9                   bankruptcy filing.
- 10                  • Significant events since the bankruptcy filing.
- 11                  • How the Plan proposes to treat claims of the type you hold (i.e., what you  
12                  will receive on your claim if the Plan is confirmed).
- 13                  • Who can vote on or object to the Plan.
- 14                  • What factors the Bankruptcy Court (the "Court") will consider when  
15                  deciding whether to confirm the Plan.
- 16                  • Why the Debtor believes the Plan is feasible, and how the treatment of  
17                  your Claim under the Plan compares to what you would receive on your Claim in liquidation.
- 18                  • The effect of confirmation of the Plan.

19                  A copy of the Debtor's Chapter 11 Plan (the "Plan") is attached hereto as  
20                  Exhibit 1. You are urged to review the Plan and, if appropriate, consult with counsel about the  
21                  Plan and its impact on your legal rights before voting on the Plan. Capitalized terms used but not  
22                  defined in this Disclosure Statement shall have the meanings assigned to such terms in the Plan  
23                  or the Bankruptcy Code.

24                  This Disclosure Statement has been prepared by the Debtor based upon its  
25                  knowledge and information in Debtor's books and records. The information contained herein  
26